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TO: Community Association Managers and Leaders
RE: N.C. Legislature Adopts Changes to HOA Statutes

It has been an extremely active legislative session for condominium and planned communities. We are pleased to report that the General Assembly has adopted some legislation this session which will significantly improve certain aspects of the law for homeowners associations and their members. Equally as significant, the legislature has not enacted legislation thus far this session which would negatively affect condominium and planned communities in North Carolina. Below, we summarize three bills which have been ratified by the General Assembly and signed into law by the Governor.

As a service to our clients, we want to keep you abreast of these and future changes in the law. There are several other bills pending which may affect HOAs, and we will report further on those should new laws be enacted.

I. Collection procedures – House Bill 331

Effective October 1, 2013, the following changes in the law are effective.

House Bill 331 represents the culmination of a 4-year effort by the NC Bar Association's Real Property Section to make the laws regarding HOA foreclosure more uniform in North Carolina through changes to G.S. 47C/47F-3-116. Hope Carmichael sits on the Section Council and chairs the Bar's HOA subcommittee which drafted this legislation. The most significant change introduced by House Bill 331 is the introduction of a designated trustee into the HOA foreclosure process – a step that has always been lacking in the interplay of the lien statutes in 47C and 47F with the power of sale foreclosure laws set out in Chapter 45.

As a practical matter, the HOA will be able to name its regular collection attorney as trustee in the Claim of Lien document. The attorney will then proceed with the foreclosure, and in the event the property is ultimately deeded following a foreclosure sale, the trustee will execute a trustee's deed, just as the mortgage foreclosure process has worked in North Carolina for decades. If the owner contests the foreclosure, including the amount owed or the obligation to pay, the Association's

attorney would recuse himself as trustee and the Association would select a new trustee who does not have a conflict of interest. The original attorney may continue to represent the Association if needed, and the \$1,200 cap on attorney's fees does not apply. This statute affords significant advantages for HOAs in that 1) Clerks in all counties across the State will have a uniform procedure to follow for HOA foreclosures; 2) lawyers, associations and homeowners will know what to expect in terms of a defined process; and 3) title passing as a result of an HOA foreclosure will be made clear following the trustee's deed.

In addition to numerous procedural provisions related to the foreclosure process itself, there are other changes enacted by House Bill 331 which affect HOAs as follows:

- The law clarifies that the Claim of Lien secures all sums due before and after the date of the Claim of Lien. This has been a gray area in the law prior to this clarification.
- Other fees and charges imposed by the association (for example, late fees, rental charges for common elements), unless otherwise stated in declaration, are enforceable under the Claim of Lien.
- The law clarifies that in sending the 15-day demand letter and Claim of Lien, the association and its attorney are entitled to rely on the address for the unit/lot owner shown on the county tax records for the unit/lot, in addition to any other absentee address which may have been provided in the Association's records. Similarly, the association may rely on a corporate entity's registered agent address as provided through the NC Secretary of State.
- The association is not required to mail the 15 Day Demand Letter or Claim of Lien to an address known to be a vacant unit/lot or to a unit/lot for which there is no US postal address.
- The association shall be entitled to recover the reasonable attorneys' fees and costs it incurs in connection with the collection of any sums due, whether collection is through foreclosure of a lien or by suit for money judgment. This clarifies and reverses a prior NC appellate decision which limited recovery of attorney's fees by an association when pursuing a money judgment as opposed to foreclosure of the lien.
- The law clarifies that unit/lot owners have the rights and remedies available to them, just like a mortgagor in Article 2A of Chapter 45 of the NC General Statutes, to enjoin mortgage sale on equitable grounds by filing a separate action in Superior Court.
- If the association, acting through its executive board in the board's sole discretion, agrees to a payment plan, attorneys' fees incurred on the account owed shall not be included or considered in calculating the \$1,200 attorney fee/trustee's commission cap.
- The statute applies to all power of sale foreclosures commenced by an association prior to October 1, 2013 and all sales and transfers of real property as part of those proceedings are valid unless an action to set aside foreclosure is commenced on or before October 1, 2013, or within a year of the sale, whichever date last occurs.

II. Amendments – HOA Governance – Limited Common Elements – Senate Bill 228

Effective October 1, 2013, this bill combines what were originally three separate bills, two of which were proposed by the Community Associations Institute and lobbied by Henry Jones on behalf of

CAI's Legislative Action Committee. While two of these changes are relatively simple in verbiage, the effect should be positive change for homeowners associations following two specific appellate cases which generated much confusion in the law.

- **Amendments:** Any amendment passed pursuant to statutory procedure in 47C or 47F or in accordance with procedure outlined in the Declaration of Covenants is presumed to be valid. This statutory provision will clarify the uncertainty regarding validity of amendments created by a prior appellate decision requiring the court to find that the substance of a covenant amendment is "reasonable."
- **Governing Documents:** So long as the legal documents are not inconsistent with the statute, the Declaration, Bylaws and Articles of Incorporation all must be considered in granting legal authority for an association. This statutory provision will clarify a prior appellate decision which negated powers granted to an association under its Articles of Incorporation where those powers were not repeated in the Declaration or Bylaws.
- **Easement of Access across Limited Common Elements:** Current law is amended to provide that the association or any owner who needs to access his lot or unit for maintenance shall have an implied easement of access across limited common elements in addition to general common elements if necessary to gain access for maintenance purposes. This legislation arose out of a unique set of circumstances in a coastal townhome community.

III. Voluntary Mediation of HOA Disputes – House Bill 278

Effective July 1, 2013, this bill codifies what has always been the law in North Carolina – prior to filing a lawsuit, an owner and association may voluntarily hire a professional mediator to try to resolve the dispute without litigation. Both parties must agree to mediate, and there is no penalty if one party proposes mediation but the other party refuses and wants to go to court instead. This bill evolved from the original proposal which would have made mediation mandatory for HOA disputes prior to a lawsuit being filed. After significant opposition to that proposal, including concerns about unconstitutionally denying access to the courts, the bill became a voluntary mediation bill. While the bill sets out procedures which can be followed if the parties agree (a full copy of the bill is attached to this memo), the most significant change for HOAs is that the association is required annually to notify its members of their right to request voluntary mediation.

For your convenience, we have drafted a template statement which can be posted on the Association's website; or, if the Association has no website, the statement should be included in the notice which is made to members of the names and addresses of board members within 30 days of the annual election (currently required by GS 47C/F-3-103). All associations should publish the following statement on the HOA website as soon as practical, or include this statement in the notice following the election of directors:

“NOTICE OF RIGHT TO VOLUNTARY MEDIATION

Pursuant to Section 7A-38.3F of the North Carolina General Statutes, all members are hereby informed that you have a right to initiate mediation pursuant to the terms of the statute to try to resolve a dispute with the Association. Both the homeowner and the Association must agree to mediate the dispute, and each side is responsible for splitting the cost of the mediation, including

payment of a professional mediator. The mediation process is an opportunity to reach an agreement to resolve a dispute – neither side gives up their right to go to court to have a judge resolve the dispute if the parties are not able to reach an agreement through mediation. The specific process to initiate voluntary mediation is outlined in Section 7A-38.3F of the North Carolina General Statutes.”

We do not believe these new changes will necessitate much change in current procedure for associations or attorneys who are already following best practices in the industry. In our firm, we have already started drafting the new forms which we will use in the uniform foreclosure process, and we do not anticipate any cost changes as a result of the new legislation. We spent many hours this summer educating legislators about the vast majority of associations who operate fairly and efficiently. We stressed the need for efficiency in HOA operations and effective collection methods for delinquent assessments. Thanks to all of you who wrote letters, made phone calls and came to speak directly with members of the General Assembly – together we were able to effectuate positive legislative changes and thwart proposed changes which threatened to go as far as elimination of the association’s right to foreclose.

As always, we will be happy to help guide you through the new processes that the law now requires. All HOAs and management companies are encouraged to review their current practices to determine how the statutory changes will affect their association operations and make the necessary changes in procedure. Please do not hesitate to contact us with any questions.